

**UNITED STATES BANKRUPTCY COURT  
DISTRICT OF DELAWARE**

In re:	)	Chapter 11
	)	
VALLEY MEDIA, INC.,	)	Case No. 01-11353(PJW)
	)	
Debtor.	)	
	)	
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THE OFFICIAL COMMITTEE OF	)	
UNSECURED CREDITORS, ON BEHALF	)	
OF VALLEY MEDIA, INC.,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Adv. Proc. No. 02-04553
	)	
CABLEVISION SYSTEMS CORPORATION	)	
and CABLEVISION ELECTRONICS	)	
INVESTMENTS, INC.,	)	
	)	
Defendants.	)	

**MEMORANDUM OPINION**

William F. Taylor, Jr.  
McCarter & English, LLP  
Mellon Bank Center  
919 N. Market Street  
Suite 1800  
P.O. Box 111  
Wilmington, DE 19899

Daniel B. Rath  
Brian E. Farnan  
Klett Rooney Lieber &  
Schorling, P.C.  
The Brandywine Building  
1000 West Street, Suite 1410  
Wilmington, DE 19801

John H. Hall, Jr.  
Shaw, Licitra, Bohner,  
Esernio, Schwartz & Pfluger, P.C.  
1475 Franklin Avenue  
Garden City, New York 11530

Counsel for Plaintiff

Counsel for Defendants

Dated: August 14, 2003

**WALSH, J.**

This opinion is with respect to Cablevision Systems Corporation and Cablevision Electronics Investments, Inc.'s (together "Defendants") motion for summary judgment (Doc. # 10) and motion to adjourn proceedings and stay discovery (Doc. # 13). The motions assert that the Official Committee of Unsecured Creditors of Valley Media, Inc. (the "Committee") lack standing to bring a derivative action to recover allegedly preferential transfers. Defendants also argue that, to the extent the Third Circuit would allow creditors to pursue derivative suits, the Committee failed to receive the required bankruptcy court approval prior to filing the adversary complaint. For the reasons set forth below, I will deny Defendants' motions.

#### **BACKGROUND**

On November 20, 2001, Valley Media, Inc. ("Debtor" and with the Committee, "Plaintiffs") filed a voluntary petition for relief under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101 et. seq. (the "Bankruptcy Code").<sup>1</sup> Since filing, Debtor has managed its business as a debtor in possession pursuant to §§ 1107 and 1108 of the Bankruptcy Code.

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<sup>1</sup> Individual sections of the Bankruptcy Code will be cited herein as "§ \_\_\_\_".

The United States Trustee appointed the Committee on December 6, 2001. The Committee instituted the present adversary proceeding on June 24, 2002 seeking turnover of approximately \$1,963,485.76 in payments for goods provided to Defendants on open account. See Doc. # 1 at ¶¶ 10-18. The complaint also seeks to avoid and recover approximately \$88,468.58 in allegedly preferential transfers. See id. at ¶¶ 38-46. Because of a conflict of interest resulting from Debtor's counsel's relationship with Defendants, the Committee, with Debtor's consent, filed the complaint for turnover and avoidance on Debtor's behalf.

In its summary judgment motion, filed on November 5, 2002, Defendants argued that the Third Circuit's panel opinion of September 20, 2002 in The Official Committee of Unsecured Creditors of Cybergene Corporation v. Chinery, 304 F.3d 316 (3d Cir. 2002), unsettled the law regarding a creditors' committee's standing to sue derivatively. Based on Cybergene, Defendants assert that the Committee lacks capacity to sue, was not a proper party to file the action and that the present adversary proceeding should be dismissed. Subsequent to the filing of the summary judgment motion, the Third Circuit vacated the Cybergene opinion and ordered a rehearing en banc. Thus, Plaintiffs responded to the motion for summary judgment by contending that the law regarding a committee's derivative

standing was settled and that the Committee had Debtor's consent to file the action.

Defendants' motion seeking adjournment and stay of discovery requests a sixty day adjournment pending the Third Circuit's rehearing and reconsideration of the Cybergenics panel opinion. See id. at ¶ 14. Plaintiffs answered Defendants' motion for adjournment and stay of discovery by requesting a denial of the motion because it was filed after the deadline for answering interrogatories and was therefore untimely.

The Third Circuit, sitting en banc, issued an opinion on May 29, 2003 in which it effectively overruled the panel decision in Cybergenics. See The Official Committee of Unsecured Creditors of Cybergenics Corporation v. Chinery, 330 F.3d 548, 580 (3d Cir. 2003)(Cybergenics II). Cybergenics II holds that under appropriate circumstances a bankruptcy court can authorize creditors committees to sue derivatively to avoid fraudulent transfers for the benefit of the estate.

#### **DISCUSSION**

With the Cybergenics II decision, Defendants' argument regarding standing is now moot. While Cybergenics II was decided in the context of a creditors' committee's standing to pursue a fraudulent conveyance action, I find nothing in the opinion to suggest that a creditors' committee's derivative

standing should be any different in the context of a § 542(a) turnover action or a § 547(b) preference action. But this does not end the inquiry into derivative standing as the Court must address Defendants' assertions that summary judgment is proper because the Committee failed to seek this Court's approval prior to filing this adversary proceeding.

The Third Circuit's Cybergenics II opinion does not set forth the exact procedures bankruptcy courts should follow in allowing creditors derivative standing. However, the Third Circuit stated that it agreed with recent Second and Seventh Circuit opinions addressing the issue. See id at 566. In In re Commodore Int'l Ltd., 262 F.3d 96, 100 (2d Cir. 2001), the Second Circuit stated the requirements for derivative standing as follows:

[W]e hold that a creditors' committee may sue on behalf of the debtors, with the approval and supervision of a bankruptcy court, not only where the debtor in possession unreasonably fails to bring suit on its claims, but also where the trustee or the debtor in possession consents.

In Fogel v. Zell, 221 F.3d 955, 966 (7<sup>th</sup> Cir. 2000), the Seventh Circuit stated the requirements for derivative standing as follows:

If a trustee unjustifiably refuses a demand to bring an action to enforce a colorable claim of a creditor, the creditor may obtain the permission of the bankruptcy court to

bring the action in place of, and in the name of, the trustee. . . . In such a suit, the creditor corresponds to the shareholder, and the trustee to management, in a shareholder derivative action.

The Second Circuit requirement is obviously a lessor requirement, but Cybergenics II did not expressly adopt it. Instead it suggests a creditors committee can be granted derivative standing when the trustee is "delinquent" in pursuing action on behalf of the estate. See Cybergenics II, 330 F.3d at 563, 568-69.

It seems to me that where, as here, a debtor's counsel has a conflict of interest in pursuing an estate claim so that it is effectively disqualified from pursuing an action which is otherwise a colorable claim, the debtor (or a trustee) can be viewed as delinquent and the creditors committee should be authorized to pursue the cause of action.

In response to Defendants' arguments regarding court approval to initiate adversary proceedings derivatively, Plaintiffs contend that approval was not required and alternatively they seek nunc pro tunc relief. Plaintiffs asserted that, should the Court find approval necessary, the approval should be granted as of the date of filing to avoid dismissal. See Doc. # 16 at ¶ 9. Nunc pro tunc relief is a form of extraordinary relief. Courts have allowed this relief

when one party is faced with the statute of limitations or where there is "little 'likelihood of confusion' as to who would file the adversary proceeding." See In re America's Hobby Ctr., Inc., 223 B.R. 275, 281-82 (Bankr. S.D.N.Y. 1998).

I find that nunc pro tunc relief is appropriate in the present adversary proceeding as dismissing it for failure to seek approval would be inefficient. I give significant weight to Debtor's consent and its reason for that consent. Of course, the complaint makes it clear that the cause of action is not direct but derivative as it is asserted "on behalf" of Debtor. On the record before me it appears that but for the conflict of interest of Debtor's counsel, Debtor would have brought this adversary proceeding itself. The Committee, involved from the beginning, was already familiar with the factual and procedural background of the chapter case. Without the Committee's participation, Debtor would have had to find outside counsel and go through a professional retention process.

These claims, if upheld, would certainly benefit the estate. In light of the potential recovery and because the Committee is in a good position to prosecute this action, nunc pro tunc relief is in the best interests of preserving assets of the estate. Absent nunc pro tunc relief, a dismissal would surely be followed by a new adversary complaint against



Defendants with the only real difference being the possibility of different counsel for the plaintiff.

#### **CONCLUSION**

For the reasons set forth above, Defendants' summary judgment motion and the motion for adjournment and stay in discovery are denied.

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**ORDER**

For the reasons set forth in the Court's Memorandum Opinion of this date:

1. Cablevision Systems Corporation and Cablevision Electronics Investments, Inc.'s ("Cablevision") Motion for Summary Judgment of Adversary Proceeding Under Bankruptcy Rules 7012, 7056 and 7071(b) (Doc. # 10), is **DENIED**.

2. Cablevision's Motion Seeking Adjournment of all Matters with Respect to this Adversary Proceeding and Stay of Discovery (Doc. # 13), is **DENIED**.

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Peter J. Walsh

Dated: August 14, 2003

United States Bankruptcy Judge